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In the

Supreme Court of the United States

OCTOBER TERM, 1979

THE GRAND BAHAMA DEVELOPMENT COMPANY, LIMITED, a Bahamian corporation, et al.,

Petitioners,

vs.

CLARENCE A. ANDERSON, et al.,

Respondents.

BRIEF IN OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI TO THE APPELLATE COURT OF ILLINOIS, FIRST DISTRICT, FIFTH DIVISION

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QUESTIONS PRESENTED

1. Is this case ripe for consideration in view of the fact that the Appellate Court's decision simply ruled that respondent's complaint stated a cause of action under federal and state securities laws.

2. Did the Appellate Court properly rule that the complaint stated a cause of action under both the state and federal securities laws.

STATEMENT OF THE CASE

This is a class action, in four counts, by respondents, certain Illinois residents, who were sold interests in un-

improved property in Lucaya, Grand Bahama Island, by the defendants. They sought relief in three counts under the Illinois Securities Law of 1953 (Ill. Rev. Stat., Ch. 121½, §§137.1 et seq.), or under the Securities Act of 1933 (15 U.S.C., §77a et seq.), because the interests purchased by respondents constituted securities, or investment contracts, within the meaning of either the Illinois or Federal Acts. Because of alleged representations and and misrepresentations, respondents sought rescission and other relief. The complaint also contained a Count IV for violation of the Interstate Land Sales Act (15 U.S.C., sec. 1709).

The trial court dismissed the first three counts relating to alleged violations of the Illinois and federal securities laws and entered an appropriate finding rendering the order final and appealable under Illinois Supreme Court Rule 304(a) [ch. 110, sec. 304(a), Ill. Rev. Stat.]. The cause remained at the trial level to adjudicate the alleged Interstate Land Sales Act violation and respondents appealed from the order dismissing the alleged securities law violations.

The Appellate Court, Fifth Division, by unanimous decision appearing in the Appendix to the Petition, reversed the order of the trial court, holding in essence that "plaintiffs (respondents here) have made the proper allegations in support of a finding that an investment contract existed so as to withstand defendants' section 45 (Illinois Civil Practice Act) motion."

Petitioners petitioned the Supreme Court of Illinois for leave to appeal from the Appellate Court's unanimous decision, and that Court by summary order, denied the petition,

SUMMARY OF THE ARGUMENT

The Appellate Court's decision means only that respondents may litigate their claims that *these defendants* promoted *the real estate in question here,* located in the Grand Bahamas, as *investments.* This case does not involve the development of real estate in any area in the United States.

The advertising and promotional materials used by the petitioners nationwide, and particularly in the Illinois area, are replete with pleas for investment money, replete with references to opportunities for both the "professional" and "non-professional" investor, replete with claims that real estate is the best hedge against inflation and the quickest and surest way to get rich, and that as the value of land in the Lucaya development goes up, and people desire that land to build houses, apartments, hotels or businesses, they must come to the people who own land to get it. The petitioners even stated that "many astute investors recognized the enormous potential here quite early in the game. Some of them have already reaped the rewards of their foresight." (E.g., C135-145, C171-172).

This case has not been decided on the merits, but only on a motion to dismiss. The Appellate Court's decision in that regard contravenes no other decision of this Court, any federal Court or any other Court to respondents' knowledge. *Woodward* v. *Terracor,* 574 F.2d 1023 (10th Cir. 1978), upon which petitioners principally rely, is wholly inappropriate because it has no relationship to the facts in this case or to the conduct of defendants in this case. Moreover, *Woodward* was decided on a motion for summary judgment where the parties had the opportunity to litigate the issues.

There is no compelling reason, in fact no reason at all, for this Court to accept review of this case at its present stages.

REASONS FOR DENYING THE WRIT

I.

THE ALLEGATIONS OF THE COMPLAINT, WHICH MUST, FOR PURPOSES OF THIS APPEAL, BE TAKEN AS TRUE, CLEARLY STATE A VIOLATION OF THE ILLINOIS AND FEDERAL SECURITIES LAWS ENTITLING PLAINTIFFS TO BE HEARD ON THE MERITS OF THE CONTROVERSY.

Respondents, on various dates and times, purchased interests in unimproved real property in Lucaya, Grand Bahama Island, from the petitioner, as evidenced by land installment contracts. What the respondents contend is that the sales, viewed in the context of the facts as hereinafter set forth, were much more than simple sales of unimproved real estate. Each sale, the respondents contend, constitutes the sale of a security.

Petitioners herein include first, The Grand Bahama Development Company, Ltd. ("Development Company"), a Bahamian corporation, which was the owner and developer of the real property involved herein. The property purchased by respondents and other similar property owned by Development Company in Lucaya, Grand Bahama Island, will be referred to herein as the "Lucaya Development".*

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* The Development Company was in reality one member of a related group of corporations involved in the building up, promotion and sale of land in the Lucaya Development. The corporate chart identifies other companies involved. Above the Development Company stands the Grand Bahama Port Authority Ltd., which negotiated a master agreement with the Bahamian government, granting special tax concessions and certain monopoly powers over the Lucaya/Freeport area, in exchange for which

America Devco, Inc. ("Devco"), a Delaware corporation, was the holding company for the United States operations of Development Company, as well as the service representative for Development Company with relation to sales of land in the Lucaya Development.

Bahama Realty Corporation ("Bahama Realty"), a Delaware corporation, was, until December 1, 1974, the holder of the exclusive sales rights in the United States for property in the Lucaya Development.

American International Realty Corporation ("American International"), an Illinois corporation, was the exclusive franchisee or agent of Bahama Realty for the sale in Illinois of property in the Lucaya Development.

Benguet Consolidated, Inc. ("Benguet"), a Philippine corporation, was the parent corporation, or a corporation related to or affiliated with Development Company, Devco and Bahama Realty. (Comp. ¶6, C3-C4; C160-C162) It is not before the Court, as it has not yet been served with process. It was succeeded, however, in December of 1973, in its role as parent corporation by Intercontinental Diversified Corp. ("IDC"), a Panamanian corporation which acquired all of Benguet's interest in Development Company, Devco and Bahama Realty. IDC is before this Court.

It is clear, and respondents do not believe it to be contested, that on a Motion to Dismiss, or motion for Judg-

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* (Continued)

it was responsible primarily for the development of the Island. The other companies also had roles to play. For example, Lucaya Country Clubs Limited ran golf courses and the Lucaya Service Co. Limited handled maintenance projects on the Island paid for by service fees collected by the Development Company.

ment on Pleadings, all of the well-pleaded facts in the Complaint must be taken as true. The complaint is quite substantial and includes a number exhibits. An affidavit was also filed in support of the complaint.

The respondents have alleged, first, in Count I:

1.-7. Identity and description of parties.

8. Development Company acquired substantially all of the real property in the Lucaya area on Grand Bahama Island.

9. Development Company caused a Master Plan for the development and usage of real property in the Lucaya Development and surrounding areas to be prepared. This Master Plan was followed.

10. Pursuant to the Master Plan, Development Company caused facilities such as schools, recreational facilities, parks, greenways, churches, waterways, water reserves, beaches, marinas, golf courses, shopping complexes and resort hotels to be constructed in and near the Lucaya Development.

11. Development Company caused roads, utilities and other improvements to be constructed on or near the lands purchased by Plaintiffs and others.

12. Development Company had final authority over advertising and promotional materials, and over the form and substance of sales contracts. More importantly, it had the authority to approve every sale, exchange or resale of land in the Lucaya Development (other than sales, exchanges or resales by a fully paid owner holding a deed subsequent to ownership by Development Company). It also had the authority to determine and set prices for and terms of the sale of property in Lucaya.

13. Petitioners instituted a large scale advertising and promotional campaign for the sale of land in the Lucaya Development through newspapers and

magazines of nationwide circulation, direct mail solicitation, group and private dinner meetings, movies and intensive personal follow ups.

14. Part of the advertising and promotional campaign included special charters to the island for on-site inspection, offers of special discounts, and offers of "free" trips to the island, all of which included guided tours, high pressure sales luncheons and compulsory visits to the sales office.

15. The advertising and promotional campaign described in paragraphs 13 and 14 was aimed at any prospective market, but particularly at professional and non-professional purchases of land for *investment purposes only.*

16. Paragraph 16 describes in a number of subparagraphs specific advertising and promotional materials, each of which actually confirms and supports respondents' claim here that the offer and the holding out of economic inducements to the respondents, were aimed at investors. They even suggested in some advertising that prospective investors should act quickly, that land was in short supply, and that some early investors in the Lucaya Development have already reaped the rewards of their foresight.

17. All of the allegations of paragraphs 8-16, can be supported by written materials, published and circulated by petitioners to respondents.

18. Many of the respondents were required to indicate on their acceptance and guarantee contract with Development Company that "I acknowledege that I expect to use this property for investment or income producing purposes and I do not expect to use it as my residence." Each of the respondents could have checked a separate acknowledgement that stated "I acknowledge that I expect to use this property as my residence." They did not do so.

19. Each of the facts alleged in Paragraphs 8-18 are representations that the purchase of land in the

Lucaya Development is an "investment" and that the Development Company will make that investment one of value by virtue of its Master Plan, the construction of community facilities and improvements to property, and its massive advertising and promotional campaign.

20. The advertising and promotional materials made it clear that the land purchased by investors such as respondents would become valuable and saleable to tourists, persons who constructed housing, and persons who established businesses, solely by virtue of the development, advertising and promotion of the island and of the Lucaya Development by Development Company. *Persons purchasing land for investment purposes could not do anything to increase the value of their investment nor was it the intention of the Development Company or the defendants that they do so.*

27-42. These paragraphs set for the allegations necessary to state a violation of the Illinois Securities Act by reason of the non-registration of the securities at the time of sale or since.

Count II of the complaint repeats and realleges many of the allegations from Count I, and then sets forth the requisite allegations of a cause of action for violation of the Federal Securities Laws, by reason of non-registration.

Count III repeats and realleges the major allegations of Count I, and then alleges violations of the antifraud sections of the Federal Securities Act. These violations include the making of many affirmative misrepresentations, *i.e.*, that there was a large and active resale market for land in the Lucaya Development, that that land would increase in value, that investors would be able to sell their investment contracts at a profit or

"trade up" to more valuable property, that other people had made substantial profits, and that Development Company's efforts would result in the Lucaya Development increasing in value without any effort on the part of investors.

Count III also alleges affirmative failures to disclose a number of important facts. Defendants failed to disclose that increases in the value of investments in the Lucaya Development were primarily dependent on the unilateral actions of Development Company in periodically increasing the prices of the Lucaya Development property. These sales prices bore no reasonable relation to the fair market value of the land. Defendants also failed to disclose that an investor desiring to resell or cash in on his investment interest would be in direct competition with the Development Company which offered favorable, long-range purchase options, and which had substantial reserves of property. Moreover, the petitioners failed to disclose that the Development Company dominated the resale market for the Lucaya Development land in that resales of land were handled by Intercontinental Realty Company, Ltd., a related corporation, which agreed with Development Company not to resell land for less than the current prices being charged by Development Company.

Though the merits of the claim set forth in Count III are at issue here only insofar as the Trial Court ruled that the facts pleaded as a matter of law did not state a claim because the interests purchased were not investment contracts or securities, it is clear that there is liability under the securities antifraud provisions for failure to disclose to a buyer the sellers' own competing interests in a market or "market making." *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972), *reh. denied,* 407

U.S. 916, *reh. denied,* 408 U.S. 931; *Chasins* v. *Smith-Barney & Co.,* 438 F.2d 1167 (2nd Cir. 1970). See also *SEC* v. *Electronics Security Corp.,* 217 F. Supp. 831 (D. Minn. 1963).

Under the facts alleged, with Development Company controlling both the primary market and the resale market, investors were really locked in to their purchases. They were unable, practically speaking, to take their loss and walk away as Intercontinental would not undersell petitioners. While theoretically free to engage private brokers to effect a sale, investors rarely were successful in doing so—in part because even if they were willing to sell at a loss, the sale still competed with the long-term favorable financing of petitioners who were selling property with down payments of as little as 5 or 10 per cent.

II.

THE DEFINITION OF WHAT CONSTITUTES AN INVESTMENT CONTRACT CLEARLY COVERS THE SUBJECT LAND INSTALLMENT CONTRACTS.

Respondents submit that the Appellate Court's decision succinctly discusses the applicable precedent controlling the definition of a security, under both the federal and state statutes. More significantly, the Court, in its Opinion, related this precedent to the instant complaint regarding *these petitioners and their alleged conduct,* not a real estate developer in any other hypothetical area under other hypothetical conditions. A few further remarks are appropriate, however.

Petitioners' great cry is that all they were doing was providing the usual "customary amenities" provided by any developer. While respondents vigorously dispute this

conclusion, they submit that at this stage of the proceeding, petitioners' characterization is irrelevant.

In the instant case, respondents purchased their properties solely for investment purposes. However, it would not have made a difference if there had been a secondary purpose of using the land for personal recreational use. In *Lowery* v. *Ford Hill Investment Co.,* 556 P.2d 1201, 1205 (Colo. 1976), the Colorado Supreme Court interpreted it *the Colorado state securities laws* to hold that a land purchase contract was a security. The court stated:

> Despite the finding by the trial court of a "secondary" purpose of personal recreational use, this subordinate motive for the purchase does not sufficiently eclipse the plaintiffs' primary purpose of an "expectation of profit."

The court concluded that while the trial court found that the "juxtaposition of purposes" presents a difficult question, it would look to the nature of the contract. It found that various aspects of that contract, irrelevant here, caused the "investment purpose to pervade the transaction". It found further, that there was no factor in that case which would remove it from the category where the purchaser was "led to expect profits *solely* from the efforts of the promoter or a third party." 556 P.2d at 1206. Certainly that is equally true here.

It has long been clear that the Illinois courts will give an expansive reading to the Illinois Securities Law so that it might serve its regulatory and protective function, and will look to the realities of a case, not merely to form.

> The courts have given the term "security" a broad construction and have held that the acts are pater-

> nalistic and hence are to be liberally construed to protect the public. In determining whether an instrument is a security within the meaning of the statute, the Courts look to the substance of the transaction, to the relationship between the parties; these elements will control as against the form of the instrument. Form is disregarded for substance and emphasis is placed on economic reality. *Polikoff* v. *Levy,* 55 Ill. App.2d 229, 234, 204 N.E.2d 807, 809 (1st Dist. 1969).

In *In Re McCormicks' Estate,* 284 Ill. App. 543, 1 N.E. 2d 769 (1st Dist. 1936), the court set forth the Illinois test for the existence of an investment contract. Though the test did not encompass the scheme in the *McCormick* case, it does encompass the scheme of the petitioners here. The question there was whether the real estate contract:

> . . . contemplated an investment of funds by the purchaser in the assets or property of the issuer with a view of receiving a profit through the efforts of the issuer." As quoted from *Brothers* v. *McMahon,* 351 Ill. App. 321, 327, 115 N.E.2d 116, 118 (1st Dist. 1953).

As we have stated heretofore, *Woodward* v. *Terracor,* 574 F.2d 1023 (10th Cir. 1978) is not controlling, persuasive or even relevant to the facts *in this case.* Moreover, the *Woodward* decision concerned a summary judgment motion.

Plaintiffs, at the very minimum, should have the right to proceed beyond the pleading stage in this case.

CONCLUSION

For the reasons given, plaintiffs submit that there is no reason whatever for this Court to accept this case for review at this stage of the proceedings.

Respectfully submitted,

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